

**DEPARTMENT OF INSURANCE  
STATE OF UTAH**

**REPORT OF EXAMINATION**

**of the**

**FIDELITY INVESTMENTS LIFE INSURANCE COMPANY**

**as of**

**December 31, 2000**



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Salt Lake City, Utah  
December 6, 2001

The Honorable Kathleen Sebelius  
Chairman, Financial Condition (EX4) Subcommittee, NAIC  
Insurance Commissioner  
State of Kansas  
Topeka, Kansas 66502

The Honorable Merwin U. Stewart  
Insurance Commissioner  
State of Utah Insurance Department  
3110 State Office Building  
Salt Lake City, Utah 84114

Commissioners,

Pursuant to your instructions and in conformity with the provisions of Utah Code Annotated (U.C.A.) and Utah Administrative Code (U.A.C.), a full scope examination has been made of the administrative affairs, books, records, and financial condition of

**Fidelity Investments Life Insurance Company**  
of  
Salt Lake City, Utah

a domestic stock company, hereinafter referred to as the "Company", as of December 31, 2000.

The following report of examination is respectfully submitted.

## **Scope of Examination**

### **Period Covered by Examination**

This examination covered the period January 1, 1997, through December 31, 2000, and included a review of material transactions and/or significant events occurring subsequent to the examination date as well as those noted during the course of this examination.

### **Examination Procedure Employed**

All phases of the examination were conducted to determine compliance with generally accepted regulatory standards and procedures in conformity with Utah Code Annotated (U.C.A) and Utah Administrative Code (U.A.C.).

Verification and valuation of assets, determination of liabilities and reserves, and an analysis and review of such other accounts and records appropriate to the examination were also performed in accordance with National Association of Insurance Commissioners (NAIC) accounting guidelines.

Various work papers, reports, certified confirmations, and other supporting documentation for the financial statements as of December 31, 2000, were provided by the certified public accounting (CPA) firm retained by the Company. These reports, workpapers and documents were utilized by the examination on a limited basis in the verification of certain balance sheet accounts and as a supplement to the procedures performed during the examination.

### **Status of Prior Examination Findings**

The prior examination was conducted by the Utah Department of Insurance, and covered the period from January 1, 1993 through December 31, 1996. Examiners from the States of Delaware and Nevada participated in the examination, representing the Northeastern (Zone 1) and Western (Zone IV), Zones, respectively.

The examination report contained no financial changes or adjustments. The prior report included three recommendations related to filing requirements, formalizing an investment service agreement, and reviewing the reserve basis for renewable term life insurance policies. These matters were addressed by the Company subsequent to the prior examination, and appropriate corrective measures were taken.

## **History**

### **General**

The Company was incorporated under the laws of the state of Pennsylvania on May 13, 1981 as Independence Square Pension Life Insurance Company. The Company's name was changed to Provident Mutual Variable Life Insurance Company on June 16, 1983. The Company was acquired by FMR Corp. on December 30, 1986, after ceding all of its in force policies to Provident Mutual Life Insurance Company of Philadelphia.

The Company's name was subsequently changed to Fidelity Investments Life Insurance Company, and it was re-domesticated from Pennsylvania to Utah effective November 10, 1992.

A review of corporate records disclosed that there were no amendments made to the articles of domestication or bylaws of the Company during the current examination period.

### **Capital Stock**

The articles of domestication provide for authorized capitalization of 1,000,000 shares of common capital stock with a par value of \$10 per share. As of December 31, 2000, there were 300,000 shares issued and outstanding with an aggregate statement value of \$3,000,000. Gross paid in and contributed surplus totaled \$63,300,000.

### **Dividends to Stockholders**

No cash or stock dividends were declared or paid during the period under examination.

## Management

The Company's articles of domestication and bylaws require a board of directors of not less than seven or more than fourteen members. The following persons were serving as directors of the Company at December 31, 2000:

<u>Name &amp; Business Address</u>	<u>Principal Business Affiliation</u>
James C. Curvey Boston, Massachusetts	Director FMR Corp.
Edward C. Johnson 3d Boston, Massachusetts	Chief Executive Officer, and Chairman of the Board FMR Corp.
Stephen P. Jonas Boston, Massachusetts	Executive Vice President, and Chief Financial Officer FMR Corp.
John J. Remondi Boston, Massachusetts	Director and Vice President Fidelity Capital Associates, Inc.
Rodney R. Rohda Boston, Massachusetts	President, Fidelity Investments Life Insurance Company
Richard A. Spillane Boston, Massachusetts	Senior Vice President Fidelity Management & Research Company
David C. Weinstein Boston, Massachusetts	Executive Vice President, Legal, and Government Affairs FMR Corp.

As of December 31, 2000, the following persons were serving as duly elected or appointed officers of the Company:

<u>Name</u>	<u>Position Held</u>
Rodney R. Rohda	President, Chairman and CEO
David J. Pearlman	Secretary and Senior Legal Counsel
Joseph L. Kurtzer Jr.	Treasurer and Vice President
William J. Johnson Jr.	Actuary and Vice President
Richard C. Murphy	Senior Vice President, Actuarial / Finance
Melanie Calzetti-Spahr	Senior Vice President, Operations
Farrell J. Dolan	Vice President, Marketing
Tai Seely Bright	Vice President, Sales
Gary L. Kelley	Vice President, Systems
Tyler W. Walton	Vice President, Client Services
Haynes L. Turkle	Vice President, System Development
Janice MacIver Drew	Vice President, Human Resources

### Committees

The board of directors established an investment committee on March 11, 1988. The committee was re-constituted under Utah Law on May 26, 1993. The committee is responsible for reviewing and ratifying all investment transactions. The Company has also established an internal "Portfolio Oversight Committee", which meets on a regular basis to review the investment portfolio and its performance.

The following individuals were serving as members on those respective committees as of December 31, 2000:

#### Investment Committee

James C. Curvey  
Rodney R. Rohda  
Richard A. Spillane

#### Portfolio Oversight Committee

Richard C. Murphy  
Joseph L. Kurtzer Jr.  
William J. Johnson Jr.  
Debbie S. Pickholtz (succeeded by Lisa J. Henaghen in 2001)

### Internal Audits

The Fidelity group of companies has its own internal audit division known as "Operations Audit and Analysis" (OAA). OAA regularly performs internal audits throughout the Fidelity group. The Company, and various areas of its operations are routinely selected to be audited through OAA's yearly audit selection process.

### Conflict of Interest Procedure

The Company does have a written conflict of interest policy. The policy requires the directors, officers, and key employees of the Company to file an annual "Disclosure of Conflicts of Interest" form which requests a declaration and disclosure of any material interest or affiliation which is in conflict or is likely to conflict with the individual's official duties at the Company.

A review of forms signed and filed during the examination period disclosed no material interests or affiliations which could be considered as a conflict or potential conflict with the subject individual's official company duties.

### Corporate Records

The actions and resolutions of the Company's board of directors and shareholders are formalized by individual written consent of the members in lieu of meetings on an annual basis. The consent forms for the examination period were reviewed, and generally included an approval of board actions during the prior year, an approval of investment transactions during the prior year, election of directors and the appointment of officers. Special actions or resolutions on matters during the interim were handled in a similar manner.

It was noted that the previous examination report, as of December 31, 1996, was reviewed by the directors of the Company.

### Affiliated Companies

The Company is a member of a holding company organization under the provisions of U.C.A. Section 31A-16-105. The Company is a direct and wholly owned subsidiary of FMR Corp., the ultimate controlling person in the organization. In addition to the Company, FMR Corp. owns approximately 123 other business entities. The following chart illustrates the direct control relationship that existed between the Company, its parent, and its subsidiary as of December 31, 2000:

#### **FMR Corp.**

Fidelity Investments Life Insurance Company

Empire Fidelity Investments Life Insurance Company

As of December 31, 2000, the voting control of FMR Corp. was allocated among the following persons:

<u>Name</u>	<u>Shares Series "A"</u>	<u>Shares Series "B"</u>	<u>Percentage</u>
Abigail P. Johnson		11,628	24.48%
Edward C. Johnson 3d		5,700	12.00
Elizabeth L. Johnson		2,641	5.56
Edward C. Johnson IV		2,641	5.56
James C. Curvey		665	1.40
49 Senior Executives own 484 shares each or 1.04%	<u>23,716</u>	<u>          </u>	<u>51.00</u>
Totals	<u>23,716</u>	<u>23,275</u>	<u>100.00%</u>

All of the above listed shares represent Common Voting Stock, with Series "A" being entitled to 51% of the voting power, and Series "B" 49% of the voting power of FMR Corp.

The Company has one wholly owned subsidiary, Empire Fidelity Life Insurance Company (Empire), which was formed during 1992. Empire is domiciled in the State of New York, and writes business only in that State.

The Company had invested \$13,500,000 in Empire, through December 31, 2000, which included contributions of \$1,000,000 in years 1998 and 2000 of the examination period. The Company's equity value in Empire as of December 31, 2000, was \$23,294,729, which was fully admitted in this report.

The Company's separate account funds include \$10,173,613,842, (78.09%) of the aggregate total, which are invested in the "Variable Insurance Products Fund", "Variable Insurance Products Fund II", and "Variable Insurance Products Fund III", all of which are open-end diversified management investment companies organized as unincorporated business trusts by Fidelity Management & Research Company, an affiliate.

A review of the Company's registration statement filings (Forms "B" and "C"), disclosed that the most recent filing was dated May 01, 2001, and was filed with the Utah Department of Insurance, by FMR Corp. on behalf of the Company.

### Service Agreements

As of December 31, 2000, the Company was party to 42 service agreements. Twelve of the agreements were with affiliated companies, which provided administrative, tax sharing, cost allocation, participation, distribution, and investment management arrangements and/or services.

The more significant affiliated agreements are summarized as follows:

1. Empire Fidelity Investments Life Insurance Company (Empire) effective: 3/10/92

This is an administrative services agreement, whereby the Company agrees to provide Empire with sufficient personnel, property, space, communication and data processing equipment to perform all accounting and administrative functions as deemed reasonably necessary for Empire to conduct its insurance operations. Provision is made for the Company to be reimbursed for the actual cost of services and facilities utilized by Empire in its operations.

2. Empire (Tax Sharing) effective: 12/31/92

This agreement provides for the filing of a consolidated federal income tax return between the Company and Empire. The terms of this agreement provide for a defined method by which the annual tax liability will be properly allocated to the extent that each Company will pay an amount, which will be equal to that which would be paid as though the two entities had filed on a separate basis. A provision is also included which requires that the subsidiary be paid for any tax credits generated by its operations, to the extent actually used in the consolidated return filed by the Company.

3. FMR Corp. and Fidelity Insurance Agency (Administrative Services) effective: 4/01/98

Under the terms of this agreement, FMR Corp., as "provider", agrees to provide Fidelity Insurance Agency, Inc. (FIA), and the Company, with the following services and resources as needed by the two companies to perform the operation of their business: accounting and tax services; legal and human resources services; telecommunication services; computer/data processing and related support; financial services, including payroll, payables, purchasing and procurement; occupancy resources, including office space, utilities and required maintenance.

The Company and FIA agree to reimburse FMR Corp. for its actual cost for the services and facilities, within 30 days of receipt of the statement of charges, which are submitted at the end of each calendar quarter.

4. FMR Corp., Fidelity Brokerage Services, Inc., National Financial Services Corporation  
effective: 3/27/00

This is an accounts receivable/payable settlement agreement involving FMR Corp, the Company's ultimate parent, Fidelity Brokerage Services, Inc., National Financial Services Corporation, and 32 other affiliates, including Empire. The agreement generally provides that all amounts currently receivable/payable by and among FMR Corp, et al., and all affiliates shall be settled and cleared exclusively through FMR Corp.

Each subsidiary shall settle its account on a monthly basis by payment to FMR Corp. of the excess, if any, of the aggregate of its accounts payable over the aggregate of its accounts receivable as of the end of the month. If any affiliate's receivables from FMR Corp. exceeds its payables as of month end, FMR Corp. will submit the net amount to the affiliate on a prompt and timely basis.

5. Fidelity Management Trust Company (FMTC) (Investment Management) effective: 7/11/97

FMTC is a Massachusetts bank and trust company which provides investment advice and management services to the Company, and acts in the capacity of "investment manager" for the Company. FMTC has the power and authority to make purchases and sales, and to execute any and all related documents on such asset accounts as designated by the Company, in accordance with investment guidelines, and within the control of the board of directors. FMTC is compensated according to a fee schedule which involves the application of various percentages being applied to the average month-end market values of the accounts at the close of the last business day at the end of each month.

6. \*Fidelity Brokerage Services, LLC., Fidelity Insurance Agency Company (FBS and FIA)  
effective: 10/01/93 (Distribution Agreement) \*(formerly Fidelity Brokerage Services, Inc.)

The Company appoints FBS as principal underwriter for the sale of all contracts. The agreement generally provides for the underwriting, marketing, sales and distribution of the Company's variable life and annuity contracts. Other affiliates involved, in addition to those listed above, include Fidelity agencies in the States of Alabama, Arizona, New Mexico, Ohio, and Texas.

The terms of the agreement generally provide for the Company to compile periodic marketing reports summarizing sales reports to FIA and FBS, and to keep them apprised of any developments in the various states with regard to registration requirements, regulatory matters, and SEC requests and amendments, and any other conditions which may effect the marketing of the insurance products. In addition, the Company and FIA will keep appropriate books and records for FBS in conformity with the rules of the 1934 Securities Exchange Act (as specified in the contract), showing all commissions paid, all initial sales of contracts, all subsequent payments made by contract owners, and any other information required by the SEC or the NASD.

Each affiliated agency agrees to be fully responsible for ensuring that no agent, representative, tele-marketer, or employee shall offer any contract on its behalf until such person is appropriately licensed and appointed by the Company

The compensation/commissions arrangements regarding the above are summarized in the individual agreements.

The Company and Fidelity Distributors Corporation (FDC) have entered into participation contracts with each of three unincorporated business trusts; the Variable Insurance Products Fund and the Variable Insurance Products Funds II, and III. (the Funds) The Company invests its separate account proceeds with these three mutual funds through FDC, an affiliated underwriter. Pursuant to the terms of the agreement, the Funds agree that their shares will be sold only to "participating insurance companies and their separate accounts", and further agree to redeem the shares of each portfolio in accordance with the prospectus provisions.

The Funds and FDC pay no fees or other compensation to the Company under this agreement. The Funds do, however, absorb the expense of printing and distribution of their own prospectuses and statements of additional information to the owners of Company issued contracts. Fidelity Management and Research Company, another affiliate, serves as the investment advisor for the Funds.

It was noted that the Company entered into an additional agreement with FDC and Variable Insurance Products III, another unincorporated business trust, during the examination period.

The overall review of contracts, indicated that they had been duly executed, and that the terms contained therein were in compliance with U.C.A. 31A-16-106.

It was noted however, during a review of Schedule "Y" in the Company's 2000 annual statement, that the schedule did not include a summary of all transactions with the parent, subsidiaries, and affiliates, as required by the annual statement instructions. The amounts reported included only those transactions between the Company and its insurance subsidiary, Empire Fidelity Life Insurance Company.

Based on the accounts receivable/payable agreement with the parent company, (FMR Corp.) effective March 27, 2000, and an overall examination review of other service contracts and administrative agreements the Company has entered into with other affiliates in the holding system, Schedule "Y" should include additional information.

#### **Fidelity Bond and Other Insurance**

The Company was a named insured on numerous insurance policies. Coverages included were commercial property, general liability, employee dishonesty, workers compensation, automobile, professional liability, and excess umbrella protection.

As of December 31, 2000, the fidelity coverage suggested by the NAIC for a company of this size and premium volume was a minimum of \$5,000,000. As of the examination date, the Company had sufficient coverage in effect, subject to a loss limit of \$100,000,000.

#### **Pension, Stock Ownership, and Insurance Plans**

Company employees are covered by a non-contributory trustee defined pension benefit plan maintained by the parent company, FMR Corp. The benefits provided are based on years of service and the employee's compensation during the past five years of service. FMR Corp. funds the deductible and charges each subsidiary for its share of contributions.

The Company also has a profit sharing plan for its employees through FMR Corp. This plan consists of two parts. The first part is an annual contribution made from available profits. The second part is comprised of employees' voluntary 401(k) contributions, voluntary after-tax contributions, and Company matching contributions to the 401(k) portion of the plan. The board of directors has reserved the right to reduce or suspend contributions subject to availability of sufficient profits and cash flows.

The Company also participates in FMR Corp.'s retirement savings plan. The Company contributes 5% of employees' eligible compensation to the plan.

The assets of the pension, profit sharing, and retirement savings plans are held under the FMR Corp. Defined Contribution Plans Trust by an affiliate, Fidelity Management Trust Company.

Certain employees of the Company are eligible for participation in the FMR Corp. Incentive Shares Plan. Under this plan, the participants receive compensation based on dividends paid on the common stock of FMR Corp. and the net increase or decrease in the net asset value of shares of common stock of FMR Corp.

On May 26, 1993, the board of directors adopted the FMR Corp. "Severance Plan". Under specified conditions, an employee who loses employment with the Company solely on account of a reduction in force or a job elimination will be entitled to severance pay.

Other benefits available to employees include medical, dental, disability, accident and life insurance coverages.

#### Statutory Deposits

As of December 31, 2000, the Company had provided the following deposits in trust in order to meet the statutory requirements for the respective states:

<u>State</u>	<u>Type of Deposit</u>	<u>Par Value</u>	<u>Market Value</u>
Arkansas	U.S. Treasury Notes	\$ 150,000	\$ 163,500
Georgia	U.S. Treasury Notes	35,000	38,150
Massachusetts	U.S. Treasury Notes	100,000	109,000
New Mexico	U.S. Treasury Notes	100,000	109,000
North Carolina	U.S. Treasury Notes	205,000	207,050
Utah	Govt. Securities	<u>2,200,000</u>	<u>2,258,000</u>
	Totals	<u>\$2,790,000</u>	<u>\$2,884,700</u>

The above listed securities were verified by direct confirmations received from their respective depositories and/or state regulatory agencies. The securities deposited on behalf of the State of Utah satisfies the Company's minimum requirement per U.C.A. Section 31A-4-105.

## **Insurance Products and Related Practices**

### **Territory and Plan of Operation**

The Company was licensed in all states, except New York, and in the District of Columbia as of December 31, 2000, and currently. The Company operates and distributes its products in the state of New York through Empire Fidelity Life Insurance Company, a wholly owned subsidiary.

The Company's marketing emphasis is concentrated on three major products; deferred variable annuities, single premium variable immediate annuities, and term life insurance. The annuity and term life insurance products are marketed, sold, and distributed through affiliated insurance agencies throughout the country. Sales are generally made by direct mail using telemarketing support, and through walk-in investment centers. As of December 31, 2000, the Company reported an estimated 1,072 agents employed for purposes of marketing its insurance products.

The deferred and variable annuity products offer investment options to the client in which the Company bears the risk. However, the majority of the Company's premium and annuity receipts are deposit funds which comprise the bulk of the variable separate account business whereby the client-investor bears the risk.

The Company's separate account business included ten Fidelity Investment mutual funds as of December 31, 1996. During the current examination period, the Company added four more Fidelity funds, and introduced fourteen additional funds from the Morgan Stanley, Warburg Pincus, PBHG, and Strong mutual fund families, in order to increase the diversification options for existing customers, and for purposes of attracting new clients.

The separate account business involving Fidelity Mutual Funds is comprised of two segregated asset accounts; the "Fidelity Investments Variable Annuity Account I", and the "Fidelity Investments Variable Life Account I". The assets of these accounts are invested in the "Variable Insurance Products Fund", the "Variable Insurance Products Fund II", and the "Variable Insurance Products Fund III". The "Funds" are all open-end, diversified management investment companies organized as unincorporated business trusts by Fidelity Management & Research Company, and managed by FMR Company, both of which are Company affiliates.

Each Fund offers a portfolio of mutual funds for investment of the separate account assets and the portfolio shares are purchased through Fidelity Distributors Corporation, an affiliated brokerage firm. Fidelity Investments Institutional Operations Company, Inc., also an affiliate, serves as the transfer agent for the portfolio shares.

The separate account business transacted in connection with the additional mutual funds, Morgan Stanley, Warburg Pincus, PBHG, and Strong, are conducted directly between the Company and the individual funds themselves. Each of these four funds are established open-end management investment companies which are available to act in the capacity as investment vehicles for separate accounts established by insurance companies in accordance with the provisions of the individual participation agreements with the Company as described in a previous section of this report.

### Policy Forms

The Company offers three basic insurance products. The largest portion of the business in force is comprised of deferred annuity contracts with fixed and variable accumulation values, and single premium immediate annuity contracts with variable and/or fixed income benefits. The Company also offers a term life insurance policy, since 1996, and in previous years, a variable life policy, which is no longer issued, and is currently in run-off status. The term life policies have guaranteed level premiums with the option of six different term plans, ranging from 5 years to 20 years.

The Company retains the first \$25,000, plus 30% of the excess over \$25,000, not to exceed \$100,000 per risk, on its term life and variable life insurance policies.

During the examination period a substantial number of options were made available to clients through the issuance of new policies and endorsements. All policy forms and endorsements were reviewed during the course of the examination, and totaled about 23 in number. All have been filed with the Utah Department of Insurance.

The Company reported 9,242 life policies, 8,822 immediate annuity contracts, and 135,864 deferred annuity contracts in force as of December 31, 2000.

### Rates

The Company's variable annuity products generally have minimum premium deposit rates of \$25,000 for single premium contracts and \$2,500 for the initial premium deposits on deferred contracts. The deferred contracts guarantee annuity purchase rates are based on the 1983 Individual Annuitant Mortality 3.0% reserve table rates. Administration charges at the separate account level are equal to 0.25%, and 0.05% of asset value, for immediate and deferred annuities respectively, and 0.75% for mortality and expense risk charges per annum. The deferred variable annuity product also provides for an annual \$30 maintenance charge. The annual maintenance charge is waived if the total premiums less any withdrawals are at least \$25,000.

### Underwriting Practices

The Company's variable products are distributed by affiliated agencies as described in a previous section of this report in accordance with provisions of various distribution agreements. The Company's term life insurance program, which was introduced during 1996, utilizes the underwriting procedures provided by LNC Administrative Services Corporation, an affiliate of Lincoln National Life Insurance Company, pursuant to an agreement effective October 29, 1996.

The physical issuance of policies, and related administrative service for the issued business is provided by Computer Sciences Corporation Inc., (formerly Financial Administrative Services, Inc.) under a third party administrative agreement effective November 11, 1996.

### Advertising and Sales Material

A review of advertising, promotional and sales literature utilized by the Company in its marketing efforts was performed during the course of the examination. There were no items or materials noted which could be considered objectionable or misleading.

### Treatment of Policyholders

During the course of the examination, a review of open and closed life and annuity claims was performed in conjunction with audit procedures related to year-end claims reserves established by the Company at December 31, 2000.

Based on this review it was concluded that the Company's processing and handling of the claims is performed as expeditiously as possible. The conclusions reached by the Company with regard to denial, compromise, and/or payment of settlements connected with the claims appeared to be fair, reasonable, and legally and technically correct.

The Company also provided the examination with copies of its policyholder complaint logs for the years 1997 through 2000. The review indicated that most of the complaints were of a routine nature, and were readily resolved by phone or a short follow-up letter. In relation to the number of policies in force, the number of complaints recorded was very small, and they were processed in an expeditious manner.

A review of files maintained at the Utah Department of Insurance disclosed that there were no complaints registered against the Company in the State of Utah during the four year examination period.

### **Reinsurance**

#### Assumed

The Company had no assumed reinsurance business as of December 31, 2000, or at any other time during the period under examination.

#### Ceded

As of December 31, 2000, the Company participated in twelve reinsurance agreements to protect the excess of its retention in all areas of coverage. The agreements are briefly summarized with regard to the reinsuring company, type of reinsurance, effective date, significant coverages, provisions, and other basic relevant information as follows:

1. Reinsurance Group of America ( St. Louis Reinsurance Company); effective date: 1/01/88

The Company retains the first \$25,000 on an automatic/facultative basis, plus 30% of the excess over \$25,000, not to exceed \$100,000 per risk on any variable life insurance policy.

2. Lincoln National Life Insurance Company; effective date: 4/01/96

The Company retains the first \$25,000 on an automatic/facultative basis, plus 30% of the excess over \$25,000, not to exceed \$100,000 per risk on various level term insurance policies.

3. Connecticut General Life Insurance Company; effective date: 10/01/94

This agreement provides for automatic stop-loss protection from excessive death benefits, under the guaranteed minimum death benefit, provided under all deferred variable annuity contracts. The agreement excludes policies where the insured person is age 70 or older, and provides a death benefit at least equal to paid premiums adjusted for withdrawals. All claims above five basis points (0.0005) of the account value are ceded to the reinsurer, subject to a maximum net aggregate insured amount of \$6,000,000 on each insured.

The Company's cost for the reinsurance is calculated quarterly at the rate of 0.15 basis points (.000015) multiplied by the sum of the contract values of all the variable annuities with the standard death benefit issued prior to 9/10/98, less the sum of the values for all insureds ages 70 and over on the calculation date, the "age adjusted aggregate contract value" (AAV) minus contract values attributable to amounts in excess of the maximum purchase amount per contract of \$6,000,000. The agreement is subject to a "treaty year deductible" of five basis points which is calculated on the last day of each treaty\* year. The deductible will be the sum of the four products obtained by multiplying each treaty quarter's AAV, as reported by the Company, times 1.25 basis points. (.000125)

\* The terms "treaty" and "agreement" are used interchangeably throughout this section, as is customary in the actual agreements.

4. Connecticut General Life Insurance Company; effective date: 10/15/93

This agreement provides for automatic excess stop-loss protection from unusually good mortality experience of insureds who have coverage under immediate variable annuity contracts. The maximum issue age is 85, and the purchase price of a new contract cannot exceed the greater of 5% of the then current aggregate annuity values under this reinsurance or \$3,000,000, unless agreed to by the reinsurer.

The Company's cost for this reinsurance is calculated annually as of each "valuation date", which is the last day of the calendar year. The calculation is based on the average aggregate reserve multiplied by 2.5 basis points. (.00025) This agreement also requires the Company to make an annual contribution to a "mortality reinsurance sidefund", which is available to reimburse the reinsurer for any net cumulative reinsurance claims under the treaty. The contribution is made on the valuation date, and is calculated by the aggregate reserve as of the valuation date, multiplied by six basis points. (0.0006)

5. Lincoln National Life Insurance Company; effective date: 1/01/88

This is a yearly renewable term reinsurance agreement. The Company retains the first \$25,000 on an automatic/facultative basis, plus 30% of the excess over \$25,000, not to exceed \$100,000 per risk on variable life insurance policies.

6. Continental Assurance Company (CNA); effective date 10/01/98

This agreement provides for automatic cession on new variable deferred annuities for the guaranteed minimum death benefit (GMDB), on policies which elect the optional ratcheting death benefit. The ratchet benefit was offered on a one time basis for contracts issued prior to 9/13/99 to policyholders whose anniversary occurred between 9/30/99 and 9/30/00. If the insured elected to add the ratchet rider, and death occurs on or before his or her 85<sup>th</sup> birthday, the death benefit will be the greater of the three following options:

- (a) The purchase payments made, less any partial withdrawals and any incurred taxes.
- (b) The contract value on the date that proof of death is received by the Company at the annuity service center.
- (c) The highest contract value on any contract anniversary on or after the contract anniversary when the ratchet rider is added to the contract and before the annuitant reaches age 80, plus any purchase payments received by the Company after such contract anniversary, reduced for any withdrawals after such contract anniversary as provided for in the rider. The ratchet rider includes a cost provision which allows the Company to deduct a mortality charge quarterly, which will be 0.05% of the contract value on the date of the quarterly charge.

The policyholder has a period of one year to accept the ratchet option. The Company's cost for the reinsurance is calculated monthly, with the premiums equal to 17 basis points, or a rate of 1.4167 basis points per month multiplied times the average account value at the end of each month. (.00014167)

Provisions "a" and "b", above, also apply to all contracts without the ratchet rider.

7. Continental Assurance Company (CNA); effective date: 9/09/98

The Company cedes and CNA automatically reinsures the GMDB on all new variable deferred annuity policies issued on or before 9/01/98 once the annuitant reaches the day after his or her 70<sup>th</sup> birthday. CNA's maximum acceptance shall not exceed \$4,000,000 on any one risk. Premium charges to the Company are 3.25 basis points, calculated monthly at the rate of 0.2708 basis points times the AAV. (.00002078) This does not include policies with the ratchet benefit.

8. Continental Assurance Company (CNA); effective date: 10/10/98

CNA automatically reinsures the GMDB on all variable deferred annuities issued after 9/09/98, with a maximum acceptance of \$4,000,000 on any one risk. Premium charges are 4.5 basis points, calculated monthly at the rate of 0.375 basis points times the AAV. (.0000375) This does not include policies with the ratchet benefit.

Effective March 01, 2000, CNA no longer reinsured the GMDB on new business for the variable deferred annuities, as the Company elected to self-insure the new policies because of cost considerations.

The Company entered into two additional reinsurance agreements in 2001. The first agreement covers GMDB on variable annuity contracts for the period March 01, 2000 to June 30, 2001 (business previously self-insured), and the second covers new business written July 1, 2001, and after.

9. Continental Assurance Company (CNA); effective date: 10/01/98

CNA automatically reinsures the GMDB on all variable deferred annuities (with the ratcheting death benefit) issued from 9/13/99 through 4/30/00. Premium charges are 16.1 basis points, calculated monthly at the rate of 1.3417 times the AAV. (.00013417)

Contracts issued after 5/01/00 are subject to premium charges of 22 basis points, calculated monthly at the rate of 1.8333 basis points times the AAV. (.00018333)

10. CNA/Munich American Reassurance Company (MARC); effective date: 4/01/98

This is a facultative coinsurance agreement, whereby the Company may submit any risk on accepted coverages in its term life policies. The Company retains the first \$25,000 of each risk, plus 30% of the excess above \$25,000 up to a maximum of \$100,000.

The reinsurer has no liability until they have made an unconditional offer (in writing) to reinsure the risk submitted by the Company.

11.&12. Principal Life Insurance Company; (2 agreements) effective dates : 2/01/99 and 4/01/99

Under the provisions of these indemnity coinsurance agreements, the Company automatically cedes 100% of the fixed annuity income portion of the policy, and the reinsurer agrees to reinsure all such benefits (including such benefits that are commuted due to the death of an annuitant). The Company pays the reinsurer premiums for reinsurance of a policy equal to the amount of the purchase payment allocated to the fixed annuity income option, less the premium taxes due on such amount. Remittances are made to the reinsurer on a daily basis.

The agreement dated 2/01/99 applies to policy forms FVIA-92100 and FVIA-99100, while the agreement dated 4/01/99 applies to policy forms FVA-88200 and NRR-96100; otherwise the language is identical.

All of the reinsurance agreements had been duly executed, and contained the usual recommended clauses and provisions for arbitration, errors and omissions, inspection of records, right of offset, termination, and insolvency.

## **Accounts and Records**

The Company prepares financial statements on both a GAAP basis and a statutory basis. An electronically posted general ledger system is maintained, consisting of a cash ledger, a statutory accrual ledger, a separate accounts ledger and a number of detailed subsidiary journals and records typically utilized by a life insurance company. At year-end the accounts comprising the three ledgers are adjusted and reclassified as appropriate, and then merged into the final statutory annual statement by a software application called a "hyperion" program.

The Company's summary ledger balances as of December 31, 2000, were trailed through the hyperion adjusting and merging process and into the year 2000 annual statement balance sheet. Additional reconciliations were performed between the 1999 and 2000 annual statement changes and traced into major annual statement exhibits for the year 2000 to the extent deemed necessary.

The Company retained a major certified public accounting firm to audit its balance sheets as of December 31, 1997, 1998, 1999, and 2000, and the related statements of income, equity and cash flows for the years then ended. Certified audit reports and accompanying financial statements and supplemental information for all of the above four years were made available to the examination, including the CPA's workpapers for the year 2000.

The Company also provided copies of an internal control review performed by the OAA during 1998, and a risk review on the handling of incoming and outgoing funds performed by Fidelity Security Services, Inc. during 2000.

The OAA review focused primarily on the adequacy and effectiveness of the internal control environment within the Company's client services and finance groups, plus an evaluation of the Company's information technology system with regard to environment, security administration procedures, disaster recovery plans, and systems and data feeds.

The review performed by Fidelity Security Services, Inc. was concentrated on the in-house handling of premium checks mailed in by clients, and check writing procedures by the Company related to disbursements.

No material weaknesses were noted in either of the reports. Company management concurred with the recommendations made, and affirmed that additional controls would be implemented in those areas which had potential for concern.

## **Financial Statements**

The financial section of this report contains the following statements and exhibits:

**Balance Sheet as of December 31, 2000**

**Summary of Operations for the Year ending December 31, 2000**

**Reconciliation of Capital and Surplus Accounts, January 1, 1997 through December 31, 2000**

Fidelity Investments Life Insurance Company  
Balance Sheet  
As of December 31, 2000

Net Admitted Assets

Bonds	\$ 277,825,678	(Note 1)
Stocks	23,294,729	
Policy loans	87,863	
Cash and short-term investments	28,782,154	
Other invested assets	-0-	(Note 2)
Amounts receivable from reinsurers	254,883	
Commissions and expense allowances	262,497	
Federal income tax recoverable and interest thereon	-0-	(Note 3)
Life insurance premiums and annuity considerations deferred and uncollected	473,250	
Investment income due and accrued	5,181,626	
Other assets non-admitted	756,518	(Note 4)
Aggregate write-ins for other than invested assets	-0-	(Note 5)
Separate Accounts	<u>13,028,534,049</u>	
Total assets	<u>\$13,365,453,247</u>	

Liabilities, Surplus and Other Funds

Aggregate reserve for life policies and contracts	\$ 50,260,224	(Note 6)
Policy and contract claims - life	135,097	
Premiums and annuity considerations received in advance	19,658	
Other amounts payable on reinsurance	939,389	
Interest maintenance reserve	34,189	
Commissions to agents due & accrued	1,090,682	
General expenses due or accrued	2,045,561	
Transfers to separate accounts	(753,207)	
Taxes, licenses and fees due or accrued	661,355	
Amounts withheld by company as agent or trustee	209,891	
Remittances and items not allocated	3,403,628	
Asset valuation reserve	266,980	(Note 7)
Payable to parent, subsidiaries and affiliates	9,910,631	
Aggregate write-ins for liabilities: Other federal income taxes	<u>-0-</u>	(Note 8)
From Separate Accounts Statement	<u>13,016,745,587</u>	
Total Liabilities	<u>\$13,084,969,665</u>	
Common capital stock	\$ 3,000,000	
Gross paid-in and contributed surplus	63,300,000	
Unassigned funds (surplus)	<u>214,183,582</u>	(Note 9)
Total Capital and Surplus	<u>\$ 280,483,582</u>	
Total Liabilities, Capital, and Surplus	<u>\$13,365,453,247</u>	

**Fidelity Investments Life Insurance Company**  
**Summary of Operations**  
**For the Year ended December 31, 2000**

Premiums and annuity considerations	\$ 406,543,029
Deposit-type funds	1,765,265,054
Net investment income	18,167,760
Amortization of Interest Maintenance Reserve (IMR)	129,159
Separate Accounts net gain from operations, excluding unrealized gains or losses	3,871,607
Commissions and expense allowances on reinsurance ceded	2,619,094
Miscellaneous income:	
Income from fees associated with investment management, administration and contract guarantees for Separate Accounts	<u>132,430,664</u>
<b>Total</b>	<b><u>\$2,329,026,367</u></b>
Death benefits	\$ 286,105
Annuity benefits	96,947,235
Surrender benefits and other fund withdrawals	750,581,103
Interest on policy or contract funds	146,449
Increase in aggregate reserves for life and A&H policies and contracts	6,764,303
<b>Total</b>	<b>\$ 854,725,195</b>
Commissions on premiums, annuity considerations and deposit-type funds (direct business only)	\$ 16,329,536
General insurance expenses	37,064,672
Insurance taxes, licenses, and fees, excluding federal income taxes	2,195,762
Increase in loading on and cost of collection in excess of loading on deferred and uncollected premiums	111,691
Net transfers to or (from) Separate Accounts	<u>1,323,605,313</u>
<b>Total</b>	<b><u>\$ 2,234,032,169</u></b>
Net gain from operations before dividends to policyholders and before federal income taxes	\$ 94,994,198
Dividends to policyholders	<u>-0-</u>
Net gain from operations after dividends to policyholders and before federal income taxes	\$ 94,994,198
Federal income taxes incurred (excluding tax on capital gains)	<u>13,391,018</u>
Net gain from operations after dividends to policyholders and federal income taxes and before realized capital gains or (losses)	\$ 81,603,180
Net realized capital gains or (losses) less capital gains tax and transferred to the IMR	<u>(1,691,774)</u>
Net Income	<b><u>\$ 79,911,406</u></b>

Fidelity Investments Life Insurance Company  
Reconciliation of Capital and Surplus Accounts  
January 31, 1997 to December 31, 2000

	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>
Capital and surplus December 31, previous year	<u>\$ 105,642,545</u>	<u>\$ 136,356,449</u>	<u>\$ 162,810,135</u>	<u>\$ 203,473,929</u>
Net Income	28,913,323	24,757,324	38,272,169	79,911,406
Change in net unrealized capital gains or (losses)	1,709,881	1,862,212	2,468,538	5,753,436
Change in non-admitted assets and related items	262,319	95,212	1,044	(12,670,341)
Change in asset valuation reserve	(171,619)	(261,062)	(77,957)	1,206,622
Aggregate write-ins for gains and losses in surplus (Other federal income taxes)	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>2,808,530</u>
Net change in capital and surplus for the year	<u>\$ 30,713,904</u>	<u>\$ 26,453,686</u>	<u>\$ 40,663,794</u>	<u>\$ 77,009,653</u>
Capital and surplus December 31, current year	<u>\$ 136,356,449</u>	<u>\$ 162,810,135</u>	<u>\$ 203,473,929</u>	<u>\$ 280,483,582</u>

## Notes to Financial Statements

### (Note 1) Bonds

\$ 277,825,678

During the course of this examination, a review of the Company's custodial agreement with the Chase Manhattan Bank disclosed that the agreement, as amended during 1997, did not include paragraph 13, of U.A.C. Rule R590-178, with regard to the banks reporting of their capital threshold on an annual basis. Prior to the conclusion of the examination, the Company and the bank executed an amendment which addressed this matter, and the custodial agreement is now in compliance with Utah Code requirements.

### (Note 2) Other Invested Assets

\$ -0-

The Company reported a single investment totaling \$1,506,930 in a limited partnership entity, which, upon review of the prospectus, appeared to have some characteristics of a joint venture.

A review of the Utah Insurance Code disclosed that this asset did not meet the criteria of U.C.A. Section 31A-17-201, Qualified Assets, or Section 31A-18-105, Permitted Classes of Investments. Therefore the reported amount was not admitted in its entirety for examination purposes.

### (Note 3) Federal Income Tax Recoverable and Interest Thereon

\$ -0-

The Company reported a tax recoverable in the amount of \$ 10,465,493. It was determined that the tax recoverable did not meet the criteria of U.C.A. Sections 31A-17-201, and 31A-18-105, for admissibility, and therefore the entire amount was not admitted per Utah Code requirements. It is noted that \$10,450,489 of the reported amount was subsequently collected by the Company during May of 2001.

### (Note 4) Other Assets not Admitted

\$ 756,518

The Company recorded an aggregate asset amount of \$1,081,646, which consisted of various component amounts of furniture, office equipment, and computer equipment and software. The aggregate amount was reported as not admitted in its entirety by the Company in the annual statement.

U.C.A. Subsection 31A-17-201 (2)(g) permits the admission of electronic and mechanical machines constituting a data processing and accounting system of which the cost is depreciated in full over a period of five years or less. As the EDP equipment reported by the Company was determined to be a qualified asset under U.C.A. Subsection 31A-17-201(2)(g), the net depreciated cost was reinstated by the examination as an admissible asset.

**(Note 5) Aggregate Write-ins for Other than Invested Assets**

**\$ -0-**

The above asset consisted of administrative fees receivable and state income taxes recoverable in the amounts of \$830,504, and \$147,012, respectively; an aggregate total of \$977,516. As neither of these items were qualified assets under the provisions of U.C.A. Sections 31A-17-201, and 31A-18-105, the entire amount was not admitted for examination purposes. It is noted that the Company recovered these amounts during 2001.

**(Note 6) Aggregate reserve for life policies and contracts**

**\$ 50,260,224**

The actuarial phase of this examination was performed by Thomas L. Burger, FSA, MAAA, of Taylor-Walker & Associates, Inc. The reserves established by the Company, as of December 31, 2000, were found to be computed in accordance with accepted reserving methods and principles, made a reasonable provision for all unpaid loss obligations of the Company under the terms of its policies and agreements, and met the requirements of the insurance laws of Utah.

The actuary recommended that the reserves for waiver-of-premium benefits under term life policies be reported in Part E of Exhibit 8, rather than in Part A, as reported by the Company.

**(Note 7) Asset Valuation Reserve**

**\$ 266,980**

The Company originally reported the above reserve at \$295,936, which was decreased by \$28,956 per examination findings.

The net decrease was the result of examination adjustments in two areas, which are summarized as follows:

1. The maximum AVR factor of 30% was applied during the years 1997 and 1998, rather than 25%, as the Company elected not to use the "Individual Method" or the "Aggregate Method" in calculating the weighted average portfolio beta of its common stock holdings.
2. The non-admission of the Cypress Tree Investment Fund, previously noted under the caption "Other Invested Assets" was also factored into the examination adjustments, which affected the years 1998 through 2000, inclusive.

Additional calculations for 1997 resulted in the transfer of \$152,247 from the default component to the equity component.

**(Note 8) Aggregate Write-ins for Liabilities (Other Federal Income Taxes)**

**\$ -0-**

The Company established a liability in the amount of \$2,808,530, as a conservative measure to provide a reserve for the difference between original tax filings and potential IRS recourse for the years 1997 through 1999 inclusive. The basis for the tax recoverables were related to dividends received deductions (DRD) and foreign tax credits (FTC) for the aforementioned years.

The liability was not recognized for examination purposes because it was not required under regulatory accounting guidelines.

(Note 9) Capital and Surplus

\$ 280,483,582

The Company's capital and surplus was determined to be \$9,355,935 less than reported. The following schedule identifies examination changes:

<u>Account/Item Description</u>	<u>Per Company</u>	<u>Per Examination</u>	<u>Changes in Surplus</u>	<u>Notes</u>
Other invested assets	\$ 1,506,930	\$ -0-	\$ (1,506,930)	(3)
Federal income tax recoverable and interest thereon	10,465,493	-0-	(10,465,493)	(4)
Other assets nonadmitted	-0-	756,518	756,518	(5)
Aggregate write-ins for other than invested assets:				
State tax recoverable	147,012	-0-	(147,012)	(6)
Fund administrative fee receivable	830,504	-0-	(830,504)	(6)
Asset valuation reserve	295,936	266,980	28,956	(7)
Aggregate write-ins for liabilities:				
Other federal income taxes	<u>2,808,530</u>	<u>-0-</u>	<u>2,808,530</u>	(10)
Total Changes			\$ (9,355,935)	
Capital and Surplus per Company			<u>289,839,517</u>	
Capital and Surplus per Examination			<u>\$280,483,582</u>	

U.C.A. Subsection 31A-5-211 (2)(a) requires the Company to maintain minimum capital in the amount of \$400,000. As of December 31, 2000, the Company's total adjusted capital was \$280,483,582 and its authorized control level risk based capital was \$6,875,899 as determined by examination findings. Prior to examination adjustments, the Company had reported total adjusted capital of \$290,135,453, and authorized control level risk based capital of \$6,930,804, pursuant to U.C.A. Subsection 31A-17-601 (7)(a).

## Summary Comments and Recommendations

Comments and recommendations resulting from examination findings are summarized as follows:

1. **Service Agreements:** A review of Schedule "Y" of the 2000 annual statement disclosed that the Company reported only those transactions with its insurance subsidiary, Empire Fidelity Life Insurance Company, and had excluded amounts transacted with FMR Corp., and other non-insurance related affiliates within the holding system.  
(See section "Service Agreements")  
  
*It is recommended that the Company report all transactions with the parent, subsidiaries, and affiliates in Schedule "Y", as required by the annual statement instructions.*
2. **Bank Custodial Agreement:** The Company's agreement with Chase Manhattan Bank, as amended during 1997, did not include paragraph 13 of U.A.C. Rule R590-178. It is noted that the Company and the bank executed an amendment to the agreement during the course of the examination, which corrected this deficiency.  
(See section "Notes to Financial Statements")
3. **Other Invested Assets:** The Company reported a single investment in a limited partnership entity, which appeared to have some characteristics of a joint venture. This asset did not meet the admissibility criteria of U.C.A. Section 31A-17-201, or Section 31A-18-105, and the entire amount was not admitted.  
(See section "Notes to Financial Statements")
4. **Federal Income Tax Recoverable and Interest Thereon:** The Company established a receivable in the amount of \$10,465,493. The entire amount was not admitted for examination purposes, as the receivable did not meet the criteria for admissibility per U.C.A. Sections 31A-17-201, and 31A-18-105. It was noted, however, that the Company did receive \$10,450,489 of the reported amount from the Internal Revenue Service during May 2001.  
(See section "Notes to Financial Statements")
5. **Other Assets not Admitted:** An examination review of the Company's non-admission of various component amounts of furniture, office equipment, and computer equipment disclosed that EDP equipment in the amount of \$756,518 was an admissible asset per U.C.A. Subsection 31A-17-201 (2)(g). This amount was reinstated as an admitted asset for examination purposes.  
(See section "Notes to Financial Statements")
6. **Aggregate Write-ins for Other than Invested Assets:** This asset consisted of administrative fees receivable and state income taxes recoverable in an aggregate amount of \$977,516. The entire amount was not admitted, as neither of the component amounts were qualified for admissibility under the provisions of U.C.A. Sections 31A-17-201, and 31A-18-105. It was noted that these receivables were subsequently recovered during 2001.  
(See section "Notes to Financial Statements")

7. Aggregate Reserve for Life Policies and Contracts: The consulting actuary made no adjustments to the reserves as reported by the Company. One recommendation was made concerning the Company's annual statement reporting of the reserves for waiver-of-premium benefits under the term life policies in Exhibit 8, Part A.  
(See section "Notes to Financial Statements")

*It is recommended that the Company report the reserves for waiver-of-premium benefits under term life policies in Exhibit 8, Part E.*

8. Asset Valuation Reserve: A review and recalculation of the asset valuation reserves from 1997 through 2000 resulted in a decrease to the reserve of \$28,956 as of December 31, 2000.  
(See "Notes to Financial Statements")

*It is recommended that future AVR calculations be performed in accordance with annual statement instructions and NAIC guidelines, and that the factors applied in calculating the annual statement components be carefully reviewed considering the Company's experience with regard to all investments subject to AVR requirements and Utah Insurance Code applications.*

9. Aggregate Write-ins for Liabilities (Other Federal Income Taxes): A liability was established in the amount of \$2,808,530 as a conservative measure to provide a reserve for the difference between original tax filings and potential IRS recourse for the years 1997 through 1999 inclusive. The liability was not recognized for examination purposes because it was not required under regulatory accounting guidelines.  
(See "Notes to Financial Statements")

10. Capital and Surplus: The Company's surplus was decreased by \$9,355,935 per net examination adjustments. The total adjusted capital and surplus per examination findings was \$ 280,483,582 as of December 31, 2000. (See "Notes to Financial Statements")

### **Conclusion**

The courteous assistance and cooperation extended by the officers, employees and representatives of the Company during the course of this examination is acknowledged and appreciated.

In addition to the undersigned, Thomas L. Burger, FSA, MAAA, of Taylor-Walker & Associates, Colette Reddoor, AFE, and Faanu Laufiso, insurance examiners representing the Utah Insurance Department, participated in this examination.

Respectfully submitted,

A handwritten signature in cursive script, reading "Jim Beckenhauer".

Jim Beckenhauer, CFE  
Examiner-in-Charge,  
representing the  
Utah Insurance Department  
and the Western Zone (IV) NAIC